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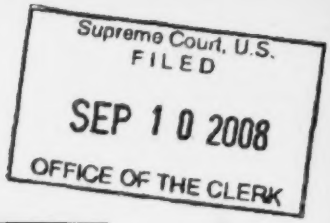

(3)

No. 08-133

IN THE

Supreme Court of the United States

THE CADLE COMPANY, PETITIONER

v.

JOSEPH M. FRIEDHEIM AND JOYCE A. FRIEDHEIM

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

REPLY BRIEF

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THIS CASE PRESENTS AN IMPORTANT QUESTION OF FEDERAL LAW

Respondents argue that, because the Fifth Circuit entered a *per curiam* ruling, "there was no decision by the Fifth Circuit on an important question of federal law." (Res. Brf. 11). This understates the impact of the *per curiam* ruling. The Fifth Circuit's decisional silence speaks volumes as to its acceptance of the decisions below.

In affirming the lower court decisions, the Fifth Circuit effectively held that "no reversible error of law appears." 5th Cir. R. 47.6. The Fifth Circuit's affirmation did not, as Respondents suggest, constitute a failure to address an important federal question in a way that conflicts with state law. (Res. Brf. 11) *See also* Sup. Ct. R. 10.

In affirming the lower court decisions, the Fifth Circuit accepted the District Court's failure to undertake an *Erie* guess as to what the Texas courts would do or certify the question on burden of proof to the Texas Supreme Court. Instead, the District Court, like the Bankruptcy Court, simply defaulted to Bankruptcy Rule 4003(c) as governing burden of proof issue – i.e., that Petitioner bore the entire burden of proof.[1]

As noted in Petitioner's principal brief, bankruptcy does not alter the burden of proof established by substantive law. (Pet. Brf. 12-18). Bankruptcy Rule 4003(c) requires that the objecting party bear the entire burden of proof. Under Texas

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[1] Petitioner also requested, by separate motion, that the Fifth Circuit certify the question to the Texas Supreme Court. The Fifth Circuit denied the motion.

law, a party claiming an exemption based on an individual retirement account - challenged by a creditor – bears the burden of proving that they are entitled to the exemption permitted Section 42.0021. *Rucker v. Rucker*, 810 S.W.2d 793, 795-96 (Tex. App. – Hous. [14th Dist.] 1991) ("It is the burden of the party claiming the exemption to prove he is entitled to it.").

By placing the entire burden of proof on Petitioner, pursuant to Bankruptcy Rule 4003(c), the Bankruptcy Court, District Court, and Fifth Circuit, not only disregarded Texas law, they departed from the well accepted and usual course of judicial proceedings, as recognized by this Court under similar circumstances. *See e.g., Raliegh v. Illinois Dept. of Revenue*, 530 U.S. 15 (2000) ("[B]ankruptcy does not alter the burden imposed by the substantive law.").[2] Burden of proof is a substantive issue which is governed by substantive law. To the extent Bankruptcy Rule 4003(c) conflicts with Texas law, Texas law on burden of proof must control.[3]

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[2] Respondents urge that the Bankruptcy Court's alternative rulings (*see* Pet. Brf. n. 2) solve the problem. (Res. Brf. 22-25). Nothing could be further from the truth. "Either/or" rulings are troubling and unfortunate. They present no legal analysis and suggest an in-security in the decision making process. In a very real sense, alternative rulings do little to promote the decision making process. A party is entitled to know what burden of proof will be applicable to the outcome of the proceeding. Otherwise, the party is unable to properly prepare its case for trial – i.e., if it has the entire burden it will likely prepare for trial one way as opposed to another. It is not enough for a trial court to say at the beginning or conclusion of the proceedings: "I do not know who has the burden. If the plaintiff does, you lose; if the defendant does, you win."

[3] Respondents boldly and arrogantly proclaim that "[b]ecause the facts of this case are so one-sided...the case would be decided in favor of Respondents no matter how the burden of proof issue was

Affirmation by the Fifth Circuit constituted acceptance of the lower court decisions on the legal issues. The legal issue is whether the correct burden of proof was initially applied to the proceedings before the Bankruptcy Court. Based on the foregoing, this case clearly presents an important question of federal law decided by the lower courts: when state law conflicts with a federal procedural rule regarding the burden of proof should a bankruptcy court be required to follow state law? The petition for writ of certiorari should be granted.

WAIVER IS A NON-ISSUE

Respondents also claim Petitioner failed to timely raise before the Bankruptcy Court the burden of proof issues presented to this Court. Respondents assert that (a) Petitioner "admitted in trial court to a different burden of proof than argued to this Court" and, therefore, "waived its arguments by failing to timely raise them" (Res. Brf. 12); (b) Petitioner "never argued at trial that the state law burden should apply or that

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resolved, [and] even if there were an important federal question decided by the Fifth Circuit, this case presents a poor vehicle for resolving it." (Res. Brf. 29). This, of course, is a merits based argument. All of the records produced at the evidentiary hearing found their source in Respondents. None of the documents proved that the IRAs at issue were qualified under the IRC. At best they proved that the Respondents had IRAs. Had the burden of proof under Texas law been applied, rather than that set forth in Bankruptcy Rule 4003(c) – as is required under this Court's precedents – the evidence, may very well have been viewed by the Bankruptcy Court in an entirely different light – i.e., Respondents (rather than Petitioner) failed to demonstrate qualification. This frames the importance of the legal issue before the Court.

the state law conflicted with Bankruptcy Rule 4003(c)...." (*Id.* 16). This assertion is incorrect.

Prior to the beginning of the evidentiary hearing on Petitioner's Objection to Exemptions, Petitioner filed *The Cadle Company's Hearing Brief (Burden of Proof)* (Bankr. Adv. Dkt. No. 78). In this brief:

- Petitioner begin by stating that "Debtors cannot establish that the IRAs are properly qualified under applicable law."
- Petitioner, relying on authorities cited before this Court (*see e.g.*, *In re Carter*, 182 F.3d 1027 (9th Cir. 1999); *In re Harrington*, 306 B.R. 172 (Bankr. E.D. Tex. 2003); *In re Mauer*, 268 B.R. 335 (Bankr. W.D. N.Y. 2001)), argued that "[i]t is only logical that the burden of proof on the issue of whether the IRAs at issue qualify as exempt under Texas law will initially lie with Debtors."
- Petitioner further argued that to not institute a shifting burden, i.e., one which required the debtor to introduce sufficient evidence to overcome the burden of persuasion, resulted in a bankruptcy system in which

> [d]ebtors could list anything as 'exempt,' produce nothing to validate the exemption, and then effectively [reverse] shift the burden to the trustee and/or other parties in interest to prove it is not properly claimed. Most creditors and trustees in an estate that has little resources or is no-asset – such as Debtor's estate – will have little capability to

> prosecute an objection if they have to bear such an initial burden. In fact, such a procedure has been labeled an 'exemption by declaration' and is not a proper approach to justice in the bankruptcy court (*citing In re Mauer*, 268 B.R. at 339 n.5).

- Petitioner further argued that "it is the debtor, not the objector who benefits from the exemption by keeping the claimed property out of the bankruptcy estate; therefore, something from the debtor substantiating the exemption, absent a bare assertion, must be necessary to prove the debtor's entitlement to it." *See In re Harrington*, 306 B.R. at 181 (holding that "in the face of an objection[,] this Court believes that a debtor must sustain a minimal burden going forward with the evidence to establish that the referenced property qualifies for the particular exemption claimed before the objecting party is obligated to go forward with its proof.").
- Finally, Petitioners concluded their hearing brief by noting that "Debtors have the initial burden of proof on the issue of whether the IRAs scheduled by Debtors qualify under applicable law."[4] Petitioners requested that

[4] In a footnote to this statement, Petitioners clearly noted that Texas law differs from Bankruptcy Rule 4003(c) in that it provides that "a party claiming an exemption under section 42.0021 bears the burden of proving that he or she is entitled to the exemption." (The Cadle Company's Hearing Brief (Burden of Proof) n.5, *citing*, Tex. Prop. Code Ann. § 42.0021; *Pillitteri v. Brown*, 165 S.W.3d

> the Bankruptcy Court require Respondents to "produce sufficient, unequivocal evidence to establish that the scheduled IRAs qualify under applicable law. Only after Debtors overcome this initial burden of production should the burden shift to Cadle."

The Bankruptcy Court overruled Petitioner's request that the initial burden of proof lie with Respondents and instead held that Petitioner had the entire burden of proof, production and persuasion, to establish that the IRAs were not qualified under applicable law. (See App. 14a – Petitioner bore "the burden of proving [by a preponderance of the evidence] that the Debtors' exemption are not properly claimed."]. In doing so, the Bankruptcy Court required Petitioner to proceed under a standard of proof which conflicts with the burden of proof standard required under Texas law, as well as the concepts of equity and fairness embodied within the Bankruptcy Code.

Based on the foregoing, it can hardly be said that Petitioner waived the burden of proof issue. This Court is not prevented from granting review on this basis.

715, 723 (Tex. App. – Dallas 2004, no pet.); *Strayhorn v. Lexington Ins. Co.*, 128 S.W.3d 772, 785-86 (Tex. App. – Austin 2004, pet. granted); *Jones v. American Airlines*, 131 S.W.3d 261, 270 (Tex. App.- Fort Worth 2004, no pet.); *Lozano v. Lozano*, 975 S.W.2d 63, 67 (Tex. App.- Houston [14th Dist.] 1998, pet. denied); *Dale v. Finance America Corp.*, 929 S.W.2d 495, 498-99 (Tex. App. – Fort Worth 1996, writ denied); *Rucker v. Rucker*, 810 S.W.2d 793, 795-96 (Tex. App. – Houston [14th Dist.] 1991, writ denied) (holding that the appellant failed to prove his entitlement to the claimed exemption because he did not establish that his retirement plan qualified under applicable provisions of the Internal Revenue Code as required by 42.0021)).

CONCLUSION

This Court should grant the instant petition for writ of certiorari. A significant and important issue of federal law is presented by this appeal, namely whether state substantive law (*i.e.*, Section 42.0021) rather than federal procedural law (*i.e.*, Bankruptcy Rule 4003(c)) should govern the issue of the applicable burden of proving a claimed exemption in bankruptcy. Alternatively, Petitioner maintains that this Court should adopt a shift in burden standard applicable to Bankruptcy Rule 4003(c) and hold that property claimed as exempt is *prima facie* exempt until the presumption of validity is rebutted. Because the Courts below adopted an incorrect standard of proof under Bankrutpcy Rule 4003(c) their decisions should be reversed and remanded for further proceedings.

Respectfully submitted,

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